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In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 968

UNION OIL COMPANY OF CALIFORNIA,
Appellant,

vs.

STATE BOARD OF EQUALIZATION OF THE STATE OF CALIFORNIA,
Appellee.

Appeal from the Supreme Court of the State of California

Motion to Dismiss or Affirm

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Appeal from the Supreme Court of the State of California

Motion to Dismiss or Affirm

Appellee, pursuant to Rule 16 of the Revised Rules of the Supreme Court of the United States, hereby moves the Court to dismiss this appeal or to affirm the judgment of the California Supreme Court, for the following reason:

There is no substantial federal question presented as a basis of jurisdiction in this Court.

QUESTION PRESENTED

The question presented by this appeal is whether it violates due process for California to impose a use tax on the lessor's use of property in California to produce rental in

come in the factual situation here present. More specifically, the question is whether it is of any constitutional significance that the transfer of possession from lessor to lessee occurred outside California or that the lessor is a corporation not qualified to do business in California when, in fact, the lessor purchased the property with the knowledge and intent that the property was to be used in California and when the property was actually principally employed for its intended purpose in California. It is the position of appellee that California can constitutionally impose a use tax under the circumstances here present just as it could constitutionally impose a property tax or an income tax with respect to the property.

We find it necessary to state at the outset that appellant's Jurisdictional Statement presents only the skeleton of the case, omitting or misstating crucial factual and legal elements vital to an understanding of the circumstances under which the California use tax was here imposed. For example, appellant fails to state that under the governing statutory provision California is precluded from imposing a use tax on a lessor's use of property in California to produce rental income unless it is found that the lessor purchased the property with knowledge and intent that such use would occur. Also ignored by appellant is that under the administrative construction of the statute, the California use tax is not applied to property purchased out-of-state and brought into California for use here unless the property is *principally* used in California in the year subsequent to its purchase.[1] It is only because these prerequisites were satisfied in the instant case that the use tax was here imposed. In fact, appellant not only fails to mention these prerequisites to

1. In some cases a six month period rather than a year is used.

application of the California use tax but instead bases its arguments on the assumption that the California use tax is to be applied to situations where neither prerequisite had been met. These and other deficiencies of appellant's Jurisdictional Statement are discussed in greater detail in the Statement of the Case and argument immediately following.

STATEMENT OF THE CASE

Appellant is a California corporation engaged in the petroleum business with its principal office and place of business in California. For many years prior to March, 1953, appellant owned and operated a fleet of tank ships which it used to transport its products to its refinery and marketing facilities located throughout California and elsewhere.

In March, 1953, appellant entered into an agreement with Cienega Tanker Corporation (a Delaware Corporation not qualified to do business in California) which provided for the sale and immediate lease-back of five of appellant's ships. The sale price was approximately $10,000,000.00, approximately $5,000,000.00 thereof being the sale price for the two vessels here involved (the S.S. Santa Paula and S.S. Lompoc). The agreement provided that the delivery and concurrent redelivery of the vessels was to take place at Astoria, Oregon, or such other port as appellant might designate. The delivery and concurrent redelivery of the two vessels here involved did, in fact, take place at Astoria, Oregon.

For purposes of the sale and lease-back, Cienega Tanker Corporation was represented in Oregon by its agent, the Joshua Hendy Corporation, a Delaware corporation qualified to do business in California. The Joshua Hendy Corporation also acted as Cienega's agent in California with

respect to the redelivery of the S.S. Santa Paula to Cienega at the end of the lease period.[2]

The S.S. Santa Paula was in use in intrastate voyages between California ports or in drydock in California 69% of the year prior to its sale and lease-back and 85% of the year following the sale and lease-back. The S.S. Lompoc was in such California use 79% of the year prior to its sale and lease-back and 92% of the year following the sale and lease-back.

Appellee assessed a use tax as to the two vessels which were principally used in California in the year subsequent to the sale and concurrent lease-back. The assessment was based on appellee's determination that, under the above circumstances, Cienega had purchased the two vessels for use in California and had made a "use" of the vessels in California within the meaning of the California Sales and Use Tax Law.[3]

The tax was collected from appellant since it was the retailer which, maintaining a place of business in California,

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2. The statement found throughout appellant's Jurisdictional Statement that Cienega had no agents or representatives in California is incorrect and overlooks paragraph IV of the Stipulation of Facts, the relevant portion of which provides.

> "Joshua Hendy Corporation, a Delaware corporation, qualified to do business in California, acted as agent of Cienega with respect to delivery of the vessels S.S. Lompoc and S.S. Santa Paula, hereinafter referred to, at Astoria, Oregon, and with respect to the redelivery of the S.S. Santa Paula at Wilmington, California, on March 18, 1955."

Although appellant states that Cienega purchased and leased the vessels in Oregon, the evidence indicates Cienega's actual "presence" in Oregon was no greater than in California.

3. The California sales tax was avoided since, as the transaction was arranged, transfer of title occurred outside California (and in a State which had no sales or use tax). There is no evidence that any State other than California has imposed a use tax with regard to these transactions.

had sold the vessels to Cienega.[1] Appellant does not dispute its liability to the State for any use tax due from Cienega with respect to the vessels. Rather, appellant's sole argument is that California could not constitutionally impose a use tax on Cienega.

NO SUBSTANTIAL FEDERAL QUESTION IS PRESENTED BY THIS APPEAL

I. Appellant Has Not Accurately Set Forth the Taxing Provisions Involved in This Case

The California use tax is imposed by section 6201 of the California Revenue and Taxation Code, which reads as follows:

> "An excise tax is hereby imposed *on the storage, use, or other consumption in this State* of tangible personal property purchased from any retailer on or after July 1, 1935, *for storage, use, or other consumption in this State* at the rate of 3 percent of the sales price of the property, and at the rate of $2\frac{1}{2}$ percent on and after July 1, 1943, and to and including June 30, 1949, and at the rate of 3 percent thereafter." (Emphasis added; Cal. Stats. 1948, p. 16)

"Use" is defined by section 6009 of that Code, as follows:

> "'Use' includes the exercise of any right or power over tangible personal property incident to the ownership of that property, except that it does not include the sale of that property in the regular course of business." (Cal. Stats. 1941, p. 533)

"Use" was purposely defined in broad terms in order that the use tax could be an effective complement to the sales tax. As stated by this Court,

> "* * * As property covered by the sales tax is exempt under the use tax, all tangible personalty sold or

1. Cal. Stats. 1941, p. 538.

> utilized in California is taxed once for the support of the state government. * * *" (*Southern Pacific Co. v. Gallagher*, 306 U.S. 167, at 171)

Appellant's principal argument in the State courts was that "use" within the meaning of the statute should be limited to "physical use." The California Supreme Court, in affirming the trial court, rejected that argument and held that if the use tax is to be an effective complement to the sales tax so as to protect against tax avoidance, "use" must include "economic use" as well as "physical use." Accordingly, a purchaser of tangible personal property who uses the property to produce rental income is making a "use" of his property within the meaning of the statute just as does the purchaser who physically uses the property himself. The Court held that the use occurs where the property is actually employed, not where the lease agreement is executed or where the lessee first takes possession of the property. In addition, whether the lessor is a resident individual or domestic corporation on the one hand or a non-resident individual or foreign corporation not qualified to do business in California on the other hand is not relevant in determining if the lessor "used" the property in California.

The above statement is a fair summary of how the California concept of "use" is interpreted with regard to persons who purchase property for the purpose of using it to produce rental income. In its attempt to demonstrate that application of the use tax to a corporation not qualified to do business in California violates due process, appellant relies on the assumption that California would impose a use tax on the out-of-state lessor whose property is brought into California by the lessee for a short period of time without the lessor's knowledge. The truth is, however, that California would not attempt to impose a use tax in that situa-

tion. This is so because of two provisions of the California use tax which appellant fails to mention.

In the first place, under the express provisions of the statute, the California use tax is only imposed with regard to property used in California which was purchased for such California use. As applied to those who purchase property for leasing purposes this "purchase for" requirement means that California would impose its use tax only on those lessors who at the time of purchase had a reasonable knowledge and intent that the property would be used in California.[5] The California use tax cannot, then, be said to be a trap for the unwary lessor whose property is, to his surprise, taken to California.[6]

Secondly, appellant has failed to mention that in situations (such as here present) where the initial use of the property for its intended purpose occurs outside California, California does not attempt to impose a use tax unless the property is actually *principally* used in California in the 12 (or sometimes six) month period following the sale. (See pages 11-12 of the Brief for Respondent in the District Court of Appeal) This point is dramatically illustrated by this very case for although Cienega purchased five vessels from appellant, the use tax was imposed only with respect to the two vessels which were principally used in California during the year following their sale and lease-back.

California would not, therefore, even attempt to impose a use tax on lessors whose property is brought into California for a short period of time.

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5. The California Supreme Court, after a careful consideration of all the relevant facts, concluded that the "purchase for" requirement had been satisfied in this case.

6. Moreover, it should not be assumed that all rented property is mobile. The question of lessor knowledge of the place of use is clearly no problem with regard to the many items of leased property which are stationary in nature.

It is the application of the California use tax, as it is written and administered, to the facts of this case that must be evaluated by this Court to ascertain if there has been a violation of due process. We submit, therefore, that the omission from appellant's Jurisdictional Statement of any mention of those provisions which are vital to an understanding of the taxing provisions here involved results in an inaccurate and misleading presentation of the issue raised on this appeal.

II. The California Use Tax, as Applied to the Facts of This Case, Does Not Violate Due Process

With regard to the power of the States to tax, due process is satisfied if there is "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." (*Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344-345) That requirement is satisfied in this case. The subject of the California use tax in the present case is Cienega's use of property in California to produce rental income. California was the State where vessels valued at $5,000,000.00 were employed to produce rental income for Cienega. It seems almost too obvious for words that California had a "definite link" or "minimum connection" with the subject of the tax.

This Court has stated that the State's connection is sufficient if the State's objective is "reasonable and just, according to our traditional conception of fair play and substantial justice." (*International Shoe Co. v. Washington*, 326 U.S. 310, 320) It cannot seriously be doubted that the California use tax here in question is "reasonable and just."

The California use tax, as interpreted by the California Supreme Court in this case, applies equally to all users of property in California. Accordingly, all persons purchasing property for use in California are required to contribute

equally to the support of the State which affords them the benefits and protections they receive by virtue of the employment of the property in this State. This is true whether the purchaser physically employs the property in California himself or whether he employs the property here to produce rental income. Certainly, the present tax is not unreasonable.

In addition, state sales taxes and their complement, the use tax, have long been recognized as reasonable sources of state revenues. In this respect, application of the use tax to lessors in situations such as here present is not only reasonable, *it is mandatory* if the use tax is to fully complement the sales tax. As stated in the opinion of the California Supreme Court:

> "As we have explained, the Legislature designed the Sales and Use Tax law as an integrated whole. Such a design is incompatible with an interpretation of the statutes [as advocated by appellant] which would leave a loophole of competitive advantage for the interstate over the intrastate lessor. The use tax, correctly applied, constitutes a legitimate expense exacted for the privilege of enjoying the advantages of the California economy."

That California is fair in its application of the use tax to lessors (whether they be resident or non-resident) is demonstrated by the fact that the tax is only imposed if the lessor purchased the property for use in California, i.e., with knowledge that the property would be utilized in California. In addition, the tax would not be imposed unless the property actually was principally used in California as explained above.

In *Wisconsin v. J. C. Penney Co.*, 311 U.S. 436, this Court, in discussing due process and State taxation, stated,

"The simple but controlling question is whether the state has given anything for which it can ask return." (311 U.S., 445)

Surely California, the State in which vessels valued at $5,000,000.00 were used to produce rental income for Cienega, can tax that use.

It is submitted that the present case falls well within the limits set by due process on the powers of state taxation as enumerated by the landmark decisions of this Court on the subject.[7]

From appellant's use of italics, it would appear that appellant's principal complaint about the application of the use tax in the present case is that Cienega, the user, was not qualified to do business in California and that the use tax is imposed on the user rather than *in rem* on the property used.[8] That contention has no merit for where there is a definite connection between the state and the subject of the tax, as there is here, it is not significant that the taxpayer is a corporation not qualified to do business in the state. The decisions of this Court dealing with the power of a state to impose an income tax on a non-resident are persuasive authority in that regard.

It is well established that California could constitutionally impose an income tax on a non-resident measured by the income from property of the non-resident here in California. (*Shaffer v. Carter*, 252 U.S. 37; *Travis v. Yale & Towne Manufacturing Company*, 252 U.S. 60; *New York ex rel.*

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7. A close parallel is found in *Stone v. Stapling Machine Co.*, 71 So. 2d 205. Appeal dismissed, 348 U.S. 802. Rehearing Denied 348 U.S. 884, which upheld a "sales tax" under circumstances similar to those here involved. This case is discussed in detail in the Brief for Respondent in the District Court of Appeal at pages 55-56.

8. Appellant concedes an *in rem* tax would be constitutional. (Juris. St. p. 7)

Whitney v. Graves, 299 U.S. 366; *International Harvester Co. v. Wisconsin*, 322 U.S. 435) In *Shaffer v. Carter, supra*, the taxpayer made the same argument as appellant makes here, namely, that a state does not have jurisdiction to impose an income tax on a non-resident even though the measure of the tax was income from sources within the taxing state. In rejecting that contention, this Court stated:

> "It is insisted, however, both by appellant in this case and by the opponents of the New York law in the *Travis v. Yale & Towne Mfg. Co.*, that an income tax is in its nature a personal tax, or a 'subjective tax imposing personal liability upon the recipient of the income' and that as to a non-resident the State has no jurisdiction to impose such a liability. This argument, upon analysis, resolves itself into a mere question of definitions, and has no legitimate bearing upon any question raised under the Federal Constitution. For, where the question is whether a state taxing law contravenes rights secured by that instrument, the decision must depend not upon any mere question of form, construction, or definition, but upon the practical operation and effect of the tax imposed." *Shaffer v. Carter*, 252 U.S. 37, 54-55)

In other words, a State has the power to tax income from sources within the State and there is no federal constitutional rule which prevents the states from exercising that power simply because the taxpayer (the person who is responsible for payment of the tax) is a non-resident. Likewise, since a State may impose a use tax with respect to use in the State (*Southern Pacific Company v. Gallagher*, 306 U.S. 167) it should not be significant that the taxpayer (user) is a corporation not qualified to do business in the State.

Appellant's argument in that regard is extremely confusing. On Page 11 of its Jurisdictional Statement, after citing

cases authorizing states to tax income of non-residents from in-state sources, appellant states:

> "But these cases go only to the power . . . to tax the income arising from a sale of property in the state . . . and do not pertain to the power to create an *in personam* liability for the tax."

That statement is nonsense. An income tax by its very terms imposes personal liability on the person earning the income. An income tax is not an *in rem* tax levied on a particular dollar which gives rise to income. Appellant's patently inconsistent statement is apparently based on its confusion regarding the power of a state to create personal liability with the power of a state to acquire *in personam* judicial jurisdiction over a non-resident defendant. The two powers involve completely independent considerations. For example, a state could enact a statute providing that owners of property located in the state are personally liable for any injury occurring to a person in the state by virtue of the dangerous condition of the property. This would obviously be a proper exercise of the state's police power. But that is entirely independent of whether a local state court could acquire *in personam* jurisdiction over a non-resident owner defendant. It may be that in such a case the plaintiff (a person injured as a result of the dangerous condition of the property) will have to sue the defendant in a federal court (on the basis of diversity of citizenship) or in the state court of the defendant's reidence. (See *Ehrenzweig, Conflict of Laws*, Part One, Section 28, page 98)

In the present case, California surely has power to legislate with regard to the use of property in the State to produce rental income and to impose a use tax with respect to such use. Cienega used the two vessels here involved in California to produce rental income. California is the state

where the use occurred and the income was earned. Certainly California's contacts with this use are no less than with the income produced by the use. The fact that Cienega was not qualified to do business in California cannot vitiate California's otherwise clearly constitutional power to tax the use.[9]

III. Appellant's Arguments Do Not Support Its Contentions

In the portion of its Jurisdictional Statement entitled "Question Presented," appellant emphasizes a matter which is wholly irrelevant to the question presented. That is, appellant stresses the fact that, as upheld by the California Supreme Court, the lessor's California use tax liability arises when the property is used in California regardless of where the particular lessor's rental agency business is located. Thus appellant states, "The use tax on the owner-lessor depends not on where he conducts *his* business, but on where the lessees conduct theirs."[10]

But since the use tax is a tax on "use," not a tax on business, doing business, or for the privilege of doing business, it would seem not only reasonable, but mandatory, that liability for a use tax arise in the state where the property is actually used. Contrary to appellant's assertion, it does not bring about an "upside down result" to have use tax liability arise in the State where the property with respect

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9. Although the question is not raised by this appeal, it would appear that California would have judicial jurisdiction over Cienega. The fact that Cienega purchased the vessels for use in California would undoubtedly satisfy the due process requirements for judicial jurisdiction set forth in *McGee v. International Life Ins. Co.*, 355 U.S. 220, and *Hanson v. Denckla*, 357 U.S. 235.

10. Even this statement is not literally correct since the use tax accrues in the State where the property is actually used to produce rental income, not necessarily where the lessee "conducts his business."

to which the tax is imposed is actually employed for its intended purpose.

It is interesting to note the apparent inconsistency in appellant's due process argument in that regard. Although appellant argues that California (the state where the leased property was actually used to produce rental income) lacks sufficient "nexus" to that use to impose a use tax, appellant has suggested in its Jurisdictional Statement and in its briefs in the California Courts that Oregon is the state which would have the power to impose a use tax because Oregon is the State in which the parties arranged for the sale and concurrent lease-back to take place.[11] But for appellant to suggest that Oregon has the power to impose a use tax on Cienega would appear incompatible with its due process argument in this case since it appears from the record herein that Cienega's sole connection with Oregon was through its agent, the Joshua Hendy Corporation, the same agent which was Cienega's representative in California. Cienega's contacts with Oregon are certainly less than with California.

The only other States which had any connection whatsoever with the sale and lease-back of the two vessels here involved are New Jersey (the State where the documents were executed) and New York (the State where the bank was located upon which appellant drew the rental payment checks). It would be a strange rule, indeed, that would allow either of those two states to impose a use tax with respect to vessels which were never once in those states, and we believe appellant would so agree. It is readily apparent therefore, that what appellant is actually seeking is im-

11. We assume appellant would contend that if the sale and concurrent lease-back took place on the "high seas", Cienega only used the vessels on the "high seas" and no state could impose a tax on the "use."

munity from *any* use tax since surely no state has more contacts with Cienega's use of the vessels to produce income than does California.[12]

Lastly, appellant states that the case here involved is contrary to two decisions of the Supreme Court of the State of Maine. Appellant fails to emphasize, however, that the decisions in those two cases are based solely on the statutes of Maine and that in those decisions the Maine Court never reached the question raised by appellant in this appeal.

In any event, it would appear that the Maine Court would reach the same result in this case as did the California Supreme Court in view of the later decision of *Automatic Canteen Co. of America v. Johnson*, 190 A.2d 734 (1963). In that case the Maine Court upheld application of the Maine use tax to an out-of-state lessor in a situation where an agent of the lessor inspected the machines while in the possession of lessees. Since in this case Cienega had an agent in California for purposes of redelivery, it is probable that the Maine Supreme Court would hold that there was a "use" in the State within the meaning of the statute. The holding of *Automatic Canteen* was affirmed by the Maine Supreme Court in the more recent decision of *Commercial Leasing, Inc. v. Johnson*, 197 A. 2d 323 (dec. Feb. 7, 1964).

In both *Automatic Canteen* and *Commercial Leasing*, the Maine Supreme Court upheld the use tax against constitutional objection. Since the Maine use tax is imposed on the user just as is the California use tax, it would appear the law of Maine is the same as California with respect to the question raised by appellant in this appeal.

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12. Neither Oregon nor New Jersey has a sales or use tax, and there is no evidence that any state other than California has imposed either a sales or a use tax with regard to these transactions.

CONCLUSION

California is the State wherein the two vessels here involved were employed in the production of rental income for Cienega. California's contacts with such use are not only substantial but greater than that of any other state. It is respectfully submitted that for California to tax such use does not violate any prohibitions imposed by due process on the power of the States to tax. Accordingly, this appeal does not present a substantial federal question and should be dismissed, or in the alternative, the judgment of the California Supreme Court should be affirmed.

Respectfully submitted,

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